

**REPORT OF THE
ASSOCIATION FINANCIAL EXAMINATION OF
SHELTER LIFE INSURANCE COMPANY**

**AS OF
DECEMBER 31, 2001**



**STATE OF MISSOURI
DEPARTMENT OF INSURANCE
JEFFERSON CITY, MISSOURI**

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Columbia, Missouri
September 17, 2003

Chairman of Financial Condition (EX4) Subcommittee
Southeastern Zone Secretary
Honorable Alfred W. Gross, Commissioner
Virginia Bureau of Insurance

Midwestern Zone Secretary
Jim Poolman, Commissioner
North Dakota Department of Insurance

Honorable Scott B. Lakin, Director
Missouri Department of Insurance
301 West High Street, Room 530
Jefferson City, Missouri 65101

Gentlemen:

In accordance with your financial examination warrant, a full scope association financial examination has been made of the records, affairs and financial condition of

Shelter Life Insurance Company

hereinafter referred to as such, as Shelter Life, or as the Company. Its administrative office is located at 1817 West Broadway, Columbia, Missouri 65218, telephone number 573-445-8441. This examination began on November 4, 2002, and concluded on the above date.

SCOPE OF EXAMINATION

Period Covered

The prior full scope association financial examination of Shelter Life was made as of December 31, 1998, and was conducted by examiners from the State of Missouri representing the Midwestern Zone of the National Association of Insurance Commissioners (NAIC), with no other zones participating.

The current full scope association financial examination covered the period from January 1, 1999, through December 31, 2001, and was conducted by examiners from the State of Missouri, representing the Midwestern Zone of the NAIC, with no other zones participating.

This examination was conducted concurrently with the examinations of the Company's parent, Shelter Mutual Insurance Company (Shelter Mutual), and its affiliates, Shelter General Insurance Company (Shelter General), and Shelter Reinsurance Company (Shelter Reinsurance).

This examination also included the material transactions and/or events occurring subsequent to the examination date, which are noted in this report.

Procedures

This examination was conducted using the guidelines set forth in the Financial Condition Examiners Handbook of the NAIC, except where practices, procedures and applicable regulations of the Missouri Department of Insurance (MDI) and statutes of the State of Missouri prevailed.

The examiners relied upon information supplied by the Company's independent auditor, PriceWaterhouseCoopers, LLP, of St. Louis, Missouri, for its audit covering the period from January 1, 2001, through December 31, 2001. Information relied upon included attorney letters, tests of controls, and narrative descriptions of processes and controls.

Comments - Previous Examination

The previous financial examination of Shelter Life was conducted by the MDI for the period ending December 31, 1998. Listed below are the comments, recommendations, and notes from the previous examination report, the Company's response, and the findings in the current examination.

Fidelity Bond

Comment: It was recommended that the Company should obtain a minimum of \$1,000,000 of fidelity coverage to cover employees for dishonest acts in the normal course of business as recommended by the NAIC guidelines for the protection of its assets.

Company's Response: The Company stated that the fidelity bond coverage had been obtained as recommended.

Current Findings: The Company currently has a financial institution bond that provides fidelity coverage in excess of the minimum level recommended by the guidelines of the NAIC. Refer to the Fidelity Bond and Other Insurance section of this report for further details.

Reinsurance

Comment: It was noted that some of Shelter Life's ceded reinsurance agreements had insolvency clauses, which did not fully comply with Missouri Regulation 20 CSR 200-2.100 (11)(A) (Credit for Reinsurance). It was recommended that the Company should review and update the insolvency clauses in its reinsurance agreements.

Company's Response: The Company stated that its ceded reinsurance contracts had been reviewed and changes were being made to have them conform with Missouri Regulation 20 CSR 200-2.100 (11)(A).

Current Findings: There were no problems found regarding the insolvency clauses in the Company's reinsurance agreements.

HISTORY

General

Shelter Life was incorporated on November 13, 1958 and was originally named M.F.A. Life Insurance Company. It was issued a Certificate of Authority and commenced business on March 2, 1959. The Company's name was changed to Shelter Life Insurance Company on July 1, 1981. The Company operates as a stock life and health insurer under the insurance laws of Chapter 376 RSMo (Life and Accident Insurance).

Capital Stock

Shelter Life is owned 100% by Shelter Mutual. The Company is authorized to issue 2,200,000 shares of common stock with a par value of \$10 per share. As of December 31, 2001, 1,200,000 shares were issued and outstanding for a total capital stock balance of \$12,000,000.

Dividends

The Company paid a \$4,000,000 dividend to Shelter Mutual in 2001. No dividends or cash distributions were paid or declared during 1999 or 2000.

Management

The management of the Company is vested in a Board of Directors that are appointed by the sole shareholder, Shelter Mutual. The Company's Articles of Incorporation and Bylaws specify that the number of directors shall be nine. The Board of Directors appointed and serving, as of December 31, 2001, were as follows:

<u>Name and Address</u>	<u>Principal Occupation and Business Affiliation</u>
James A. Offutt Osage Beach, MO	Chairman, Retired Executive Shelter Insurance Companies
Robert W. Maupin% Columbia, MO	Vice Chairman, Retired Executive Shelter Insurance Companies
Raymond E. Jones Columbia, MO	Executive Vice President and Secretary Shelter Insurance Companies
H. Marshall Chatfield Columbia, MO	Retired Executive Kansas City Life Insurance Company
Ann K. Covington Columbia, MO	Attorney / Partner Bryan Cave, LLP
John D. Duello Rocheport, MO	President and Chief Executive Officer Shelter Insurance Companies
Andres Jimenez Madrid, Spain	Vice President and Chief Executive Officer Mapfre Re Compania de Reaseguros, S.A.
John W. Lenox* Columbia, MO	Retired Executive Shelter Insurance Companies
Barry L. McKuin Morrliton, AR	President Morrliton Area Chamber of Commerce

* Mr. Lenox died in November 2002 and was replaced by Don A. McCubbin in April 2003
% Mr. Maupin retired in April 2003 and was replaced by Dr. Gerald Brouder in May 2003

Committees

The Bylaws require an Executive and Compensation Committee and an Audit Committee of the Board of Directors. The Bylaws also allow for other committees to be appointed by the Board of Directors as needed. An Investment Committee was in operation during and subsequent to the examination period. As of December 31, 2001, the members of each committee were as follows:

Executive and Compensation Committee

Robert W. Maupin, Chairman
J. Donald Duello
H. Marshall Chatfield
James A. Offutt
Ann K. Covington

Audit Committee

Barry L. McKuin, Chairman
Ann K. Covington
H. Marshall Chatfield

Investment Committee

J. Donald Duello, Chairman
Raymond E. Jones
Thomas Fischer
John W. Lenox
Robert W. Maupin
James A. Offutt
H. Marshall Chatfield

Officers

The officers elected by the Board of Directors and serving as of December 31, 2001, were as follows:

John D. Duello	President and Chief Executive Officer
Raymond E. Jones	Executive Vice President and Secretary
Robert T. Cox #	Executive Vice President and General Counsel
Don A. McCubbin	Executive Vice President - Underwriting
Jerry L. French	Vice President, Treasurer and Assistant Secretary
Patricia A. McDonald	Vice President and General Manager
Max T. Dills @	Vice President – Actuarial
Thomas N. Fischer	Vice President – Investments
Gary L. Ford	Vice President – Planning and Research
William C. Keithley	Vice President – Information Services
Ricky L. Means **	Vice President – Claims
John D. Moore	Vice President – Marketing
Joe L. Moseley	Vice President – Public Affairs
Gary D. Myers ***	Vice President – Administration
Donald H. Northway	Vice President – General Services
L. Gerald Brooks	Assistant Treasurer
Donald W. Hagen	Assistant Secretary

Robert T. Cox resigned effective March 1, 2002 and was replaced by Randa C. Rawlins on April 15, 2002. Ms. Rawlins was appointed as General Counsel only.

@ Max T. Dills was elected as Vice President – Administration on February 21, 2002. S. Daniel Clapp was elected Vice President – Actuarial on that date also.

** Ricky L. Means was elected Vice President – Underwriting on February 21, 2002. Patrick D. Gruber was elected Vice President – Claims on that date also.

*** Gary D. Myers was elected Executive Vice President on February 21, 2002.

Conflict of Interest

The Company has a policy that requires all officers, directors, and key employees to complete a conflict of interest statement each year. Signed statements of officers and directors were reviewed for the examination period. No significant exceptions were noted.

Corporate Records

A review was made of the Articles of Incorporation and Bylaws for the examination period. There were no amendments or changes to the Articles of Incorporation during the period under examination. The Bylaws were amended in April 2001 to require an Audit Committee to be maintained.

The minutes of the Board of Directors' meetings, committee meetings, and stockholders' meetings were reviewed for proper approval of corporate transactions. In general, the minutes appear to properly reflect and approve the Company's major transactions and events for the period under examination.

Acquisitions, Mergers and Major Corporate Events

None.

Surplus Debentures

No surplus debentures were issued or outstanding for the period under examination.

AFFILIATED COMPANIES

Holding Company, Subsidiaries and Affiliates

The Company is a member of an Insurance Holding Company System as defined by Section 382.010, RSMo (Definitions). An Insurance Holding Company System Registration Statement was filed by the parent, Shelter Mutual, on behalf of itself, Shelter Life, and its other insurance subsidiaries, for each year of the examination period.

Shelter Mutual, a property and casualty insurer, does not have any stockholders or controlling entity due to its formation as a mutual entity. The Company is ultimately owned by the policyholders of Shelter Mutual. Affiliated insurers that are also owned 100% by Shelter Mutual include Shelter Reinsurance, an international reinsurance company, and Shelter General, a property and casualty insurer.

Shelter Life has partial ownership of the following subsidiaries:

Shelter Financial Services, Inc. (SFS) – A holding company for Shelter Benefits Management, Inc.

Shelter Benefits Management, Inc. (Shelter Benefits) – Provides the human resource function and manages agent and employee benefits for the Shelter Insurance Companies.

Shelter Enterprises, LLC – This is a small entity (only \$6.1 million of total assets) that owns property and equipment and derives its income from leasing the assets to affiliates, including Shelter Mutual, and non-affiliates.

Daniel Boone Underwriters, LLC – An insurance broker that places risks from leads generated by agents of the Shelter Insurance Companies. The risks placed are in lines of business that are not written by Shelter Mutual or Shelter General.

Daniel Boone Agency, Inc. – An insurance broker in the same manner as explained for Daniel Boone Underwriters, LLC above, except that this entity operates in Illinois only.

DBU, Inc. – An insurance broker in the same manner as explained for Daniel Boone Underwriters, LLC above, except that this entity operates in Mississippi only.

The operations of the Company's other affiliates are described as follows:

Shelter Financial Corporation (SFC) – A holding company for Shelter Bank.

Shelter Bank – A savings and loan company that sells certificates of deposits, individual retirement accounts, and provides auto loans and mortgage loans. It does not have any demand accounts (checking or savings). Its customers are mainly policyholders of Shelter Mutual and Shelter General, but customers may also come from the general public.

Shelter (UK) Holdings, Ltd. – A holding company for Shelter Dedicated, Ltd. and Commodore Underwriting Agencies, Ltd.

Shelter Dedicated, Ltd. – A Lloyd's of London corporate member that accepts risks for a Lloyd's syndicate. Accepted risks for the policy year from January 1, 2001 through December 31, 2001. Due to the poor experience, no other risks were accepted after 2001. The company is now in run-off with a three-year accounting period ending December 31, 2003.

Commodore Underwriting Agencies, Ltd. (Commodore) – An underwriter for risks taken by Shelter Dedicated, Ltd and other Lloyd's syndicates. As of the first quarter of 2003, the entity has no operations, employees, or significant assets.

Organizational Chart

The following table depicts Shelter Life's ownership and holding company system, as of December 31, 2001:

<u>Company</u>	<u>Parent or Controlling Entity</u>	<u>Ownership</u>
Shelter Mutual Insurance Company	Policyholders	100%
Shelter General Insurance Company	Shelter Mutual Insurance Company	100%
Shelter Enterprises, LLC	Shelter General Insurance Company	45%
	Shelter Life Insurance Company	45%
	Shelter Reinsurance Company	10%
Shelter Life Insurance Company	Shelter Mutual Insurance Company	100%
Shelter Reinsurance Company	Shelter Mutual Insurance Company	100%
Shelter (UK) Holdings, Ltd.	Shelter Reinsurance Company	100%
Shelter Dedicated, Ltd.	Shelter (UK) Holdings, Ltd.	100%
Commodore UW Agencies, Ltd.	Shelter (UK) Holdings, Ltd.	100%
Shelter Financial Corporation	Shelter Mutual Insurance Company	100%
Shelter Bank	Shelter Financial Corporation	100%
Shelter Financial Services, Inc.	Shelter Mutual Insurance Company	79.5%
	Shelter General Insurance Company	11%
	Shelter Life Insurance Company	9.5%
Shelter Benefits Management, Inc.	Shelter Financial Services, Inc.	100%
Daniel Boone Underwriters, LLC	Shelter Mutual Insurance Company	40%
	Shelter General Insurance Company	40%
	Shelter Life Insurance Company	20%
Daniel Boone Agency, Inc.	Daniel Boone Underwriters, LLC	100%
DBU, Inc.	Daniel Boone Underwriters, LLC	100%

Intercompany Transactions

Shelter Life had the following intercompany transactions during the examination period:

- On May 13, 1999, Shelter Life and Shelter Mutual executed an Exchange Agreement in which Shelter Mutual transferred twenty-four corporate bonds and cash with a combined value (market value plus accrued interest) of \$100,223,532 to Shelter Life. In exchange, Shelter Life issued a \$100,223,532 promissory note to Shelter Mutual. The promissory note was subsequently assigned to Shelter Benefits, as part of a Transfer and Assumption Agreement, effective May 19, 1999. The Transfer and Assumption Agreement is described in the Intercompany Agreements section of this report.
- Shelter Life sold structured settlements to Shelter Mutual and Shelter General during the examination period. The structured settlements were used to provide periodic payouts of claim payments due under the terms of policies issued by Shelter Mutual and Shelter General. The claimants are the beneficiaries of the contracts. Shelter Mutual and Shelter General collectively purchased \$3,500,000, \$4,000,000, and \$2,500,000 of structured settlements from Shelter Life during 1999, 2000, and 2001, respectively.

Intercompany Agreements

The Company's intercompany agreements in effect, as of December 31, 2001, are outlined below.

- 1. Type:** Agreement for Management Services and Facilities
Affiliate: Shelter Mutual
Effective: January 1, 1997
Terms: Shelter Mutual agrees to provide the employees to operate all aspects of Shelter Life. Services to be provided include recordkeeping, processing, planning, budgeting, receipt and disbursement activities, and all work incidental to the operation of Shelter Life's business. Shelter Mutual agrees to provide office space, utilities, computer systems, office equipment, and supplies. In exchange for the services and facilities provided by Shelter Mutual, Shelter Life will make monthly payments to Shelter Mutual. Payments will be calculated in accordance with the Joint Expense Allocation Agreement between Shelter Mutual and the Subsidiaries.

2. Type: Joint Expense Allocation Agreement

Affiliates: Shelter Mutual, Shelter General, Shelter Reinsurance, SFS, Daniel Boone Underwriters, LLC, Shelter Enterprises, LLC, Daniel Boone Agency, Inc., DBU, Inc., Shelter Benefits

Effective: May 19, 1999

Terms: Each party agrees to pay its direct expenses in instances when each entity's actual usage can be determined. The parties agree to allocate any joint expenses for instances in which the identification and segregation of each entity's actual share is not practically feasible. The allocation methodologies for each category of joint expenses are as follows:

- (1) Personnel – estimated or actual time
- (2) Real Estate – square footage and employee count
- (3) Investment – portfolio value
- (4) Claims Adjustment (applicable to Shelter Mutual and Shelter General only) – incurred losses
- (5) Other Expenses – assets, employee count, or written premium

3. Type: Transfer and Assumption Agreement

Affiliates: Shelter Mutual, Shelter General, Shelter Benefits

Effective: May 19, 1999

Terms: Shelter General and Shelter Life paid \$3,124,245 and \$636,571, respectively, to Shelter Mutual for the purpose of transferring both companies agent termination pay liabilities. Shelter Mutual transferred certain agent liabilities and employee benefit liabilities totaling \$95,223,532, as of May 19, 1999, to Shelter Benefits. The liabilities transferred included agents termination benefits, post-retirement benefits, accrued vacation benefits, and director's retirement plan benefits. In exchange, Shelter Mutual assigned its rights to the \$100,223,532 promissory note issued by Shelter Life to Shelter Benefits. Shelter Benefits also issued 500,000 shares of preferred stock, with a total par value of \$5,000,000 to Shelter Mutual. Finally, Shelter Benefits agrees to assume future agent liabilities and employee benefit liabilities from Shelter Mutual.

4. Type: Tax Allocation Agreement

Affiliates: Shelter Mutual, Shelter General, Shelter Reinsurance, SFS, SFC, Shelter Benefits, Shelter Bank

Effective: No stated effective date. Applicable to 1999 and subsequent tax years.

Terms: Shelter Mutual will file a consolidated federal income tax return on behalf of itself and its subsidiaries. The tax liability for each company will be the amount that would have been determined on a separate filing basis. The subsidiaries will pay their share of tax payments to Shelter Mutual within 10 days following any tax payments made by Shelter Mutual. Shelter Mutual will refund any amount due to the subsidiaries within 10 days after filing the consolidated return.

Shelter Life is a named insured on a general liability insurance policy issued by Shelter Mutual. The policy insures the premises and operations of the Shelter Mutual and all named insureds. Premium for this policy is charged to Shelter Life through intercompany allocations under the Joint Expense Allocation Agreement.

Intercompany Payments

The following table summarizes the payments made during the exam period, between Shelter Life and its affiliates, pursuant to intercompany agreements.

Affiliate	Agreement	Net Paid / (Received)		
		1999	2000	2001
Shelter Mutual	Joint Expense Allocation	\$7,678,375	\$7,639,825	\$8,082,643
Shelter Mutual	Tax Allocation	875,067	5,944,408	7,456,923
Shelter Benefits	Transfer and Assumption	502,380	2,210,616	366,978
TOTAL		\$9,055,822	\$15,794,849	\$15,906,544

FIDELITY BOND AND OTHER INSURANCE

The Shelter Insurance Companies are named insureds on a financial institution bond. The bond provides employee fidelity coverage with a liability limit of \$2,500,000 and a \$50,000 deductible. This level of coverage complies with the suggested minimum amount of fidelity insurance according to NAIC guidelines.

The Shelter Insurance Companies are also named insureds on the following insurance policies: property, general liability, umbrella excess liability, automobile physical damage and liability, aircraft physical damage and liability, workers compensation and employers liability, computer crime, kidnap and ransom / extortion, and earth movement.

PENSION, STOCK OWNERSHIP AND INSURANCE PLANS

Shelter Life does not have any direct employees or agents. Employees and agents of the parent, Shelter Mutual, perform all functions necessary for the operation of Shelter Life, pursuant to the Agreement for Management Services and Facilities. Shelter Life reimburses Shelter Mutual for an allocated share of the payroll and benefits costs of the employees that provide services, pursuant to the Joint Expense Allocation Agreement. Both agreements are described further in the Intercompany Agreements section of this report.

A variety of standard benefits are provided to the Shelter Mutual employees and agents. These benefits include, but are not limited to, the following: medical insurance, dental insurance, life insurance, personal accident insurance, disability insurance, sick leave, and tuition reimbursement. Employees are also provided with a defined benefit pension plan and a 401(k) savings and profit sharing plan. Certain highly compensated employees are provided with a Supplemental Employee Retirement Plan (SERP).

STATUTORY DEPOSITS

Deposits with the State of Missouri

The funds on deposit with the Missouri Department of Insurance as of December 31, 2001, as reflected below, were sufficient to meet the capital deposit requirements for the State of Missouri in accordance with Section 376.290 RSMo (Trust Deposits). The funds on deposit as of December 31, 2001, were as follows:

<u>Type of Security</u>	<u>Par Value</u>	<u>Fair Value</u>	<u>Statement Value</u>
U.S. Treasury Bonds	\$2,500,000	\$3,150,935	\$2,496,569

Deposits with Other States

The Company also has funds on deposit with other states. Those funds on deposit as of December 31, 2001, were as follows:

<u>State</u>	<u>Type of Security</u>	<u>Par Value</u>	<u>Fair Value</u>	<u>Statement Value</u>
Arkansas	Corporate Bond	\$500,000	\$629,454	\$509,232

INSURANCE PRODUCTS AND RELATED PRACTICES

Territory and Plan of Operation

Shelter Life is licensed as a life, accident and health insurer by the Missouri Department of Insurance under Chapter 376 RSMo (Life and Accident Insurance). The Company is licensed and writes business in Missouri and 12 other Midwestern states, as follows:

Arkansas	Indiana	Kentucky	Nebraska
Colorado	Iowa	Louisiana	Oklahoma
Illinois	Kansas	Mississippi	Tennessee

The states with the largest percentage of 2001 direct written premiums and annuity considerations were Missouri (33% of total) and Arkansas (18% of total). The major lines of business for Shelter Life, based upon 2001 net written premiums, are as follows:

<u>Line of Business</u>	<u>Percentage of Total Net Written Premiums</u>
Ordinary Life	65.3%
Individual Annuities	10.5%
Group Accident and Health	13.3%
All Other	<u>10.9%</u>
Total	100.0%

The Company's products are marketed by approximately 1,400 captive agents, which also produce business for the parent, Shelter Mutual, and two affiliates, Shelter General and Shelter Bank. Shelter Mutual also has a marketing staff that uses various methods of advertising and direct mailings to promote the products of Shelter Life and affiliates.

Policy Forms & Underwriting
Advertising & Sales Materials
Treatment of Policyholders

The Missouri Department of Insurance has a market conduct staff that performs a review of these issues and generates a separate market conduct report. The most recent MDI market conduct examination report was dated April 7, 2000, and covered the period from January 1, 1999 to December 31, 1999. No significant problems were noted from review of this report.

REINSURANCE

General

The Company's premium activity on a direct written, assumed and ceded basis, for the period under examination, is detailed below:

	<u>1999</u>	<u>2000</u>	<u>2001</u>
Direct Business	\$88,503,421	\$90,426,908	\$95,596,527
Reinsurance Assumed	0	0	0
Reinsurance Ceded:			
Affiliates	0	0	0
Non-affiliates	<u>(2,078,103)</u>	<u>(2,558,944)</u>	<u>(2,879,995)</u>
Net Premiums Written	<u>\$86,425,318</u>	<u>\$87,867,964</u>	<u>\$92,716,532</u>

Assumed

The Company does not assume any business.

Ceded

The Company is contingently liable for all reinsurance losses ceded to others. This contingent liability would become an actual liability in the event that an assuming reinsurer fails to perform its obligations under the reinsurance agreement.

The Company has an automatic coinsurance agreement, effective December 1, 1999, with Business Men's Assurance Company (BMA), that covers the Company's ordinary 10, 20 and 30 year, level term policies. Shelter Life's retention is 50% of the face amount of each policy with a maximum retention of \$400,000 per policy. A jumbo limit of \$20,000,000 applies to any one insured.

The Company has a reinsurance agreement, effective January 1, 1994, with Employers Reassurance Corporation (ERAC), that covers all of the Company's individual life risks. Shelter Life retains the first \$400,000 of risk for covered policy. ERAC's reinsurance limit is \$1,000,000 per policy. One exception applies to the 10, 20 and 30 year, level term policies, which are also covered under the BMA automatic coinsurance agreement. For these term policies, ERAC assumes the excess over the Company's \$400,000 maximum retention.

In addition to the automatic coinsurance agreements, the Company also has facultative agreements for life policies with ERAC, BMA, Transamerica Occidental Life, Canada Life Assurance Company, and Reinsurance Group of America.

The Company has a coinsurance agreement with Employers Reinsurance Corporation, effective January 1, 1991, that covers personal accident and sickness policies. Retention and liability limits vary depending on the type of coverage and loss year. For individual disability income, the Company's retention is 40% of loss during the first three years and 8% of loss thereafter with a reinsurance limit of \$4,500 per month for the first three years and \$6,900 per

month thereafter. For group long-term disability, the agreement is a 50% quota share agreement with a reinsurance limit of \$1,500 per month per individual loss.

The Company has a coinsurance agreement with Indianapolis Life Insurance Company (ILIC), effective November 30, 1997. The agreement is in effect a fronting arrangement in which the Company sold a survivor life insurance product developed by ILIC using policy forms and marketing materials also developed by ILIC. The business from these policies is ceded 100% to ILIC. The Company discontinued issuing policies under this agreement, effective January 1, 2002.

The Company had a catastrophe excess of loss agreement with Reliastar Life Insurance Company, effective April 1, 2001. The Company had a retention of \$800,000 for each catastrophic accident occurring during the term of the agreement with a reinsurance limit of \$10,000,000 per event. A catastrophic event is defined as the death of three or more insureds caused by one event or occurrence. This agreement was terminated April 1, 2002.

Shelter Life has a new two-layer, catastrophe reinsurance agreement, effective April 1, 2002, with various reinsurers. The first layer coverage is \$6,000,000 in excess of the Company's retention of \$1,000,000 per catastrophic event. Manulife Reinsurance is ceded 100% of the first layer coverage. A second layer of coverage is provided through a group of reinsurers consisting of Manulife Reinsurance, BMA, RMG Specialty Underwriters, and Q.B.E. International Insurance Limited. The second layer coverage is \$30,000,000 in excess of the Company's retention of \$7,000,000 per event.

ACCOUNTS AND RECORDS

General

The CPA firm, PricewaterhouseCoopers, LLP, of St. Louis, Missouri, issued audited statutory financial statements of the Company for all years in the examination period.

The actuarial opinion regarding the Company's policy and claim reserves was issued by Donald W. Hagen, FSA, MAAA, for all years in the examination period. Mr. Hagen is an actuary employed by Shelter Mutual, but works exclusively on the operations of Shelter Life.

FINANCIAL STATEMENTS

The following financial statements, with supporting exhibits, present the financial condition of Shelter Life for the period ending December 31, 2001. Any examination adjustments to the amounts reported in the financial statements and/or comments regarding such are made in the "Notes to the Financial Statements." The failure of any column of numbers to add to its respective total is due to rounding or truncation.

There may have been additional differences found in the course of this examination, which are not shown in the "Notes to the Financial Statements." These differences were determined to be immaterial concerning their effect on the financial statements, and therefore, were only communicated to the Company and noted in the workpapers for each individual Annual Statement item.

Assets as of December 31, 2001

	<u>Assets</u>	Non-Admitted <u>Assets</u>	Net Admitted <u>Assets</u>
Bonds	\$629,626,248	\$ 0	\$629,626,248
Preferred Stocks	9,013,806	0	9,013,806
Common Stocks	53,488,157	0	53,488,157
Policy Loans	30,580,830	0	30,580,830
Cash and Short-term Investments (Note 1)	12,492,185	0	12,492,185
Other Invested Assets	2,795,066	0	2,795,066
Agg. Write-ins for Invested Assets:			
Policy Liens	207,487	95,196	112,291
Amounts Recoverable from Reinsurers	555,262	0	555,262
EDP Equipment and Software	102,771	0	102,771
Guaranty Funds Receivable or on Deposit	1,979,015	776,770	1,202,245
Life Insurance Premiums and Annuity Consid. Deferred and Uncollected	10,383,501	0	10,383,501
A&H Premiums Due and Unpaid	1,121,008	0	1,121,008
Investment Income Due and Accrued	11,600,262	0	11,600,262
Receivable from Parent, Sub., and Affiliates	83,975	0	83,975
Other Assets Non-Admitted	8,117	8,117	0
Agg. Write-Ins for Other than Invested Assets:			
Miscellaneous Receivables	<u>6,818</u>	<u>0</u>	<u>6,818</u>
TOTAL ASSETS	<u>\$764,044,508</u>	<u>\$880,083</u>	<u>\$763,164,425</u>

Liabilities, Surplus and Other Funds as of December 31, 2001

Aggregate Reserve for Life Policies and Contracts	\$411,905,397
Aggregate Reserve for A&H Policies (Note 2)	17,748,078
Liability for Deposit-Type Contracts	62,876,712
Policy and Contract Claims – Life	4,056,456
Policy and Contract Claims – Accident and Health	3,148,139
Policyholders' Dividends Due and Unpaid	2,734
Policyholders' Dividends Payable in Following Year	4,305,630
Premiums Received in Advance	215,407
Interest Maintenance Reserve	642,181
General Expenses Due or Accrued	2,614,225
Taxes, Licenses and Fees Due or Accrued	352,996
Federal Income Taxes Due or Accrued	3,443,978
Unearned Investment Income	42,537
Amounts Withheld or Retained	188
Remittances and Items Not Allocated	192,111
Asset Valuation Reserve	7,403,403
Payable to Parent, Subsidiaries and Affiliates	105,896,744
Aggregate Write-Ins for Liabilities:	
Reinsurance Premiums Due to Reinsurers	44,013
Miscellaneous Payables	2,245
TOTAL LIABILITIES	\$624,893,174
Common Capital Stock	12,000,000
Unassigned Funds (Surplus)	126,271,251
Capital and Surplus	<u>\$138,271,251</u>
TOTAL LIABILITIES AND SURPLUS	<u>\$763,164,425</u>

Summary of Operations For the Year Ended December 31, 2001

Premiums and Annuity Considerations	\$92,716,532
Considerations for Supp. Contracts with Life Contingencies	185,930
Net Investment Income	39,027,771
Amortization of Interest Maintenance Reserve	142,085
Commission and Expense Allowances on Reins. Ceded	900,434
Miscellaneous Income	<u>6,826</u>
TOTAL	\$132,979,578
Death Benefits	18,577,264
Matured Endowments	170,881
Annuity Benefits	4,423,648
Disability Benefits and Benefits Under A&H Policies	20,556,402
Surrender Benefits and Withdrawals for Life Contracts	14,058,051
Interest and Adjust. on Policy or Deposit-Type Contract Funds	3,034,528
Payments on Supp. Contracts with Life Contingencies	401,887
Increase in Aggregate Reserves for Life, A&H Policies	(7,121,047)
Commissions on Direct Business	5,504,955
General Insurance Expenses	15,926,096
Insurance Taxes, Licenses and Fees	1,784,663
Increase in Loading on Deferred and Uncollected Premiums	243,194
Aggregate Write-Ins for Deductions:	0
Structured Settlements Transferred	<u>36,678,452</u>
TOTAL	<u>\$114,238,974</u>
NET GAIN FROM OPERATIONS	\$18,740,604
Dividends to Policyholders	4,572,698
Federal Income Taxes Incurred	5,936,089
Net Realized Capital Gains Transferred to the IMR	<u>3,593,447</u>
NET INCOME	<u>\$11,825,264</u>
CAPITAL AND SURPLUS:	
Capital and Surplus, December 31, 2000	\$137,182,980
Net Income	11,825,264
Change in Net Unrealized Capital Gains or (Losses)	(5,499,814)
Change in Deferred Income Tax	1,879,230
Change in Non-Admitted Assets	(681,603)
Change in Asset Valuation Reserve	3,450,733
Cumulative Effects of Changes in Accounting Principles	(5,885,538)
Dividends to Stockholders	<u>(4,000,000)</u>
CAPITAL AND SURPLUS, DECEMBER 31, 2001	<u>\$138,271,252</u>

Notes to the Financial Statements

Note 1 – Cash and Short-Term Investments

\$12,492,185

Commercial paper investments of Shelter Mutual, Shelter General, and Shelter Life are commingled in a single investment account with Merrill Lynch. The total cost basis of the account was \$50,421,557, as of December 31, 2001. The Company represented that \$9,945,791 of the account value was attributable to Shelter Life. Pooled investments are allowed pursuant to Section 379.083 RSMo (Investment Pools). However, the pooled investments must meet the requirements of this statute and a pooling agreement must be in place. Shelter Life does not have a pooling agreement with Shelter Mutual or Shelter General. The Company is directed to immediately submit a pooling agreement to the MDI for prior approval, as required by Section 379.083 RSMo, and ensure that the agreement complies with this statute.

Note 2 – Aggregate Reserve for Accident and Health Policies

\$17,748,078

The Company did not perform a Gross Premium Valuation for its individual A&H line of business, as of December 31, 2001, to determine the extent of future losses for this line of business. Identified losses would require a premium deficiency reserve to be established.

Based upon the recommendation of MDI's consulting actuary, Milliman USA, the Company is directed to perform a gross premium valuation in the future. Premium deficiency reserves should be calculated in accordance with SSAP No. 54 (Individual and Group Accident and Health Contracts) and Appendix A-010 (Minimum Reserve Standards for Individual and Group Health Insurance Contracts) of the Accounting Practices and Procedures Manual.

Examination Changes

None.

General Comments and/or Recommendations

Pooled Investments (page 24)

Commercial paper investments of Shelter Mutual, Shelter General, and Shelter Life are commingled in a single investment account with Merrill Lynch. Pooled investments are allowed pursuant to Section 379.083 RSMo (Investment Pools). However, the pooled investments must meet the requirements of this statute and a pooling agreement must be in place. Shelter Life does not have a pooling agreement with Shelter Mutual or Shelter General. The Company is directed to immediately submit a pooling agreement to the MDI for prior approval, as required by Section 379.083 RSMo, and ensure that the agreement complies with this statute.

Gross Premium Valuation (page 24)

Based upon the recommendation of MDI's consulting actuary, Milliman USA, the Company is directed to perform a gross premium valuation for its individual A&H line of business. Any premium deficiency reserves that result should be calculated in accordance with SSAP No. 54 (Individual and Group Accident and Health Contracts) and Appendix A-010 (Minimum Reserve Standards for Individual and Group Health Insurance Contracts) of the Accounting Practices and Procedures Manual.

ACKNOWLEDGMENT

The assistance and cooperation extended by the officers and the employees of Shelter Mutual Insurance Company during the course of this examination is hereby acknowledged and appreciated. In addition to the undersigned, Shawn Hernandez, CFE, Shannon Schmoeger, CFE, Steve Koonse, CFE, Mark Nance, CFE, Andy Balas, CFE, Barbara Bartlett, and James Smith, examiners for the Missouri Department of Insurance, also participated in this examination. The firm of Milliman USA, also participated as a consulting actuary.

VERIFICATION

State of Missouri)
)
County of)

I, Tim L. Tunks, on my oath swear that to the best of my knowledge and belief the above examination report is true and accurate and is comprised of only facts appearing upon the books, records or other documents of Shelter Life Insurance Company, its agents or other persons examined or as ascertained from the testimony of its officers or agents or other persons examined concerning its affairs and such conclusions and recommendations as the examiners find reasonably warranted from the facts.

Tim L. Tunks, CPA, CFE
Examiner-In-Charge
Missouri Department of Insurance

Sworn to and subscribed before me this _____ day of _____, 2003.

My commission expires: _____

Notary Public

SUPERVISION

The examination process has been monitored and supervised by the undersigned. The examination report and supporting workpapers have been reviewed and approved. Compliance with NAIC procedures and guidelines as contained in the Financial Condition Examiners Handbook has been confirmed.

Frederick G. Heese, CFE, CPA
Audit Manager
Missouri Department of Insurance